50th Anniversary Year

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TAX·FEATURES

Tax Freedom Day Is May 4!

2 Hour, 43 Min. Tax Bite From U.S. Worker's Day To Pay 1987 Tax Bill

Taxes will take a 2-hour, 43-minute bite from the average worker's 8-hour earnings in 1987. That's up from 2-hours, 39-minutes in 1986.

Federal taxes will claim 1 hour and 46 minutes of a worker's earnings, while state-local taxes preempt 57 minutes' worth of productive labor. The total tax bite from the workday is far ahead of the next most costly item, housing and household operation, which will require a worker to put in 1 hour and 27 minutes on the job, a minute less than in 1986. Third come food and tobacco, which will consume an hour's worth of work, the same time span as last year.

Researchers at the Tax Foundation detect only minor shifts in the allocation of a day's pay over the last year. Earning the money for the clothing budget will require 23 minutes on the job — the same as in 1986. Other items requiring the same time on the job this year as last include medical expenses (39 minutes), transportation (42 minutes), and recreation (21 minutes).

The higher tax bill this year means that less earning time is available for "miscellaneous" costs, a catch-all category comprising personal care, personal business, private education, religious and welfare activities, net foreign travel, and net savings. This year, the worker will have 3 minutes fewer in the daily 8 hours to work for these items.

The 2-hour, 43-minute tax bite means that today's total tax burden per 8-hour day for 1987 is exactly the same as it was in 1981 prior to the impact of "ERTA" — the Economic Recovery Tax Act of 1981. ERTA caused a drop in the Federal portion of the tax burden, lessening the work times required to cover taxes in 1982, 1983, and 1984. (See Tax Freedom Day story in adjacent column.) This year the cycle comes full course, as subsequent increases in Federal business and payroll taxes have eroded some of the gain from ERTA, and as the total tax take has increased apace with the economic rebound.

The lowest bite from a U.S. worker's eight hours on the job in this decade occurred in 1984, when workers put in 2 hours, 36 minutes to cover their tax bills. That time allocation broke down into 1 hour, 42 minutes for Federal taxes and 54 minutes for state-local collections. Tax Foundation analysts say that, with talk of higher taxes in Washington and the increased need for additional levies at the state-local levels, we are unlikely to enjoy such levels in the foreseeable future. See page 3 for detailed chart.

May 4 is Tax Freedom Day 1987. It takes the average American from January 1 through May 3 to pay the tax collector, assuming every dollar in the paycheck is paid out for Federal, state and local government taxes from the first day of the year.

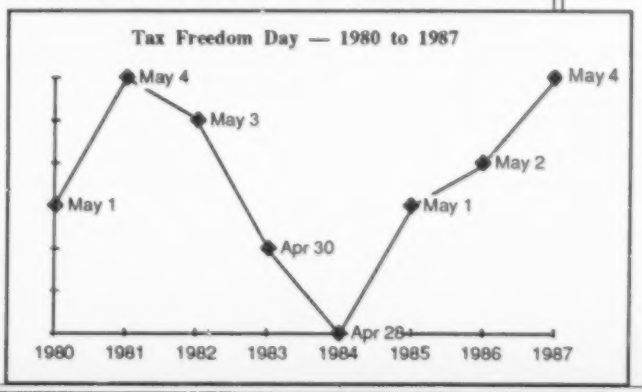
Economists at the Tax Foundation annually calculate Tax Freedom Day as a way of showing how government dominates the economy. That presence is still growing. Since 1984, the date has moved six days farther on in the calendar--from April 28 to May 4. Tax Freedom Day has advanced two days in just the past year, according to revisions based on updated government data. Tax Freedom Day, 1986, fell on May 2.

This year, the American taxpayer has returned to the same point he was at prior to passage of the Economic Recovery Tax Act of 1981 (ERTA). That legislation stopped the on-going rise of Federal taxes and Uncle Sam's tax take dropped slightly relative to time worked until 1985, when it rose again.

The full impact of ERTA's cuts were never felt. They were diminished by subsequent Congressional take-backs of business tax cuts in 1982 and 1984, higher excise taxes on gasoline and cigarettes, and hikes in payroll taxes instituted to restore the troubled Social Security system to solvency.

At the state-local levels, taxes have generally risen faster than incomes over the past seven years, taking up any slack taxpayers may otherwise have temporarily enjoyed from Federal cuts. The net result is that we are back where we were before ERTA — to a May 4 date for Tax Freedom Day.

The average taxpayer also pays more because of the economy's continuing recovery. Tax collections have risen along with the expanding economy and growing incomes of Americans, causing the flow of revenues to Federal, state and local treasuries to increase as well.



THIS ISSUE:

PAGE 1:
Tax Freedom Day

Tax Bite

PAGE 2:
Medicare's Growth

Federal Tax Burden

PAGE 3:
"Front Burner"

INSERT:
1987 State Tax Prospects

The Medicare Miracle: It Grows When It's Cut

Medicare is one of the biggest and fastest-growing Federal programs. At the rate things are going, within a few years, one out of every ten dollars in the budget will be spent on Medicare alone. Moreover, recent proposals by President Reagan to expand Medicare's coverage for catastrophic illness are likely to spur additional spending increases in the years ahead. Yet, despite Medicare's size and growth, Congress has claimed more than $30 billion in deficit reduction through recent cutbacks in this program. By explaining how Medicare has grown when it has been cut, this article shows why it has been so difficult to make genuine, lasting deficit and spending reductions.

Growth in Spending

In its 20 years of operation, Medicare has greatly improved access for elderly to health services. More than 30 million persons (including 3 million who are eligible on account of disability) are covered by Medicare. But this protection comes with a very high price tag. The following table shows how Medicare has ballooned from a modestly priced program when it was launched in the late 1960s into one of the most costly Federal obligations:

	1967 actual	1972 actual	1977 actual	1982 actual	1987 est.	1992 proj.
Outlays	$3.4	$8.8	$21.5	$50.4	$78.1	$139.1
% Total Outlays	2.2%	3.8%	5.3%	6.8%	7.7%	10.6%
%GNP	0.4%	0.8%	1.1%	1.6%	1.7%	2.2%

Medicare has grown much more steeply than both the overall economy and total Federal outlays. As a result, Medicare spending has almost quadrupled its share of Federal outlays, from about 2 percent in the late 1960s to almost 8 percent at the present time. Similarly, Medicare has grown from less than 1/2 percent of gross national product (GNP) to almost 2 percent. These trends might accelerate in the years ahead, even if Medicare benefits are not enhanced. The Congressional Budget Office's (CBO) baseline projection of the Federal budget under current policy shows Medicare accounting for 10 percent of outlays and 2 percent of GNP in 1992.

Cost escalation has been due to a number of factors. One has been the growing number of elderly, adding more than half a million to the Medicare rolls each year. Another is that inflation is much steeper in the health sector than in the overall economy. In 1986, the general inflation rate was only about 1 percent, but the cost of health services rose about 7 percent. A third factor has been increased utilization of services, because of technological advances and the installation of costly equipment.

Exaggerated Cutbacks

Congress has been grappling with Medicare for the past decade and it has claimed a great deal of success in controlling the costs of this program. In fact, Congress has taken credit for cutting Medicare in six of the seven years since 1980; it enacted two Medicare cutting laws in 1986. In line with congressional claims, recent full-page newspaper ads sponsored by more than 100 interest groups protested that "during the past 5 years, more than $30 billion has been cut from Medicare and Medicaid." (Medicaid is the health-care program for low-income persons.) The trend data depict a different

(Continued on page 3)

1987 Tax Burden Reaches $818 Billion; CA, NY, and TX Bear Heaviest Loads

The ink may be dry on tax reform, but there has been no reform in the Federal government's voracious appetite for more tax money. The Feds will collect almost $818.9 billion in taxes during fiscal year 1987, say economists at the Tax Foundation. This is based on the Administration's 1988 budget presented in January 1987, which projects the 1987 figure to surpass 1986 taxes by $74.3 billion, a ten percent increase.

The effect of the Tax Reform Act of 1986 (TRA86) on income tax distribution is demonstrated by the $41.6 billion jump in corporate taxes projected for 1987, a whopping 65.9 percent increase over the $63.1 billion collected in 1986, while individual income taxes will creep up only 4.3 percent, to $364.0 billion. Social insurance levies will grow to $296.9 billion, a 6.3 percent rise, and the take from all other taxes will remain almost constant, at $53.2 billion.

The estimates for 1988 show further growth: $12.4 billion in additional corporate taxes, $28.8 billion from individuals, and $32.7 billion for social insurance purposes.

California, New York, and Texas hold the questionable honor of having the highest tax burdens in the nation, as they have for many years. Just ten states will send more than 58 percent of all the money the Federal government collects in taxes, even though these states house less than 54 percent of the population. These "top ten" account for $477.5 billion in taxes. In descending order, they are:

CA	$101.4 billion
NY	$ 70.7 billion
TX	$ 57.4 billion
IL	$ 43.4 billion
PA	$ 39.8 billion
FL	$ 39.3 billion
OH	$ 35.2 billion
NJ	$35.0 billion
MI	$31.2 billion
MA	$23.9 billion

These ten states (plus the District of Columbia) represent only 3 percent of the population and bear less than 3 percent ($22.8 billion) of the Federal tax burden:

ME	$ 3.1 billion
DC	$ 2.9 billion
AK	$ 2.6 billion
ID	$ 2.6 billion
DE	$ 2.5 billion
MT	$ 2.2 billion
ND	$ 2.0 billion
SD	$ 1.8 billion
WY	$ 1.7 billion
VT	$ 1.5 billion

The ten states with the highest per capita tax burdens will kick in $218.9 billion in taxes, about 26.7 percent of the 1987 total. The average tax burden for their residents will be $4,100 — 22 percent higher than the national average of $3,365. Approximately 6.8 percent of the tax burden will be borne by people from the ten states with the lowest per capita burdens, amounting to some $55.4 billion. Their average burden will be $2,393 — close to 29 percent below the average for the nation as a whole.

"Top Per Capita"		"Bottom Per Capita"	
CT	$ 4,904	NM	$2,535
DC	$ 4,680	AL	$2,515
NJ	$ 4,588	ID	$2,505
AK	$ 4,520	SD	$2,473
MD	$ 4,122	KY	$2,466
MA	$ 4,093	SC	$2,406
NY	$ 3,962	WV	$2,356
DE	$ 3,896	AZ	$2,355
IL	$ 3,757	UT	$2,341
NH	$ 3,701	MS	$2,031

The table on page 4 provides details of both the total and per capita tax burdens by state, estimated by Tax Foundation economists for fiscal year 1987.

Tax Features

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State Tax and Fiscal Prospects, 1987

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The 49 states holding regular legislative sessions in 1987 are facing a heavy volume of tax bills that could lead to a near-record level of statutory tax increases. (Only Kentucky is not holding a regular session.)

Pending measures in 29 states would raise taxes by between $7 billion and $8 billion annually, according to a Tax Foundation survey in mid-March. If approved, this would represent the biggest legislative increase in revenues since the $8 billion increase in 1983.

According to proponents, the new revenues are needed primarily to raise spending for public education and highways, to offset revenue shortfalls due to poor economic performance and declining oil revenues, and to shore up state financial reserves.

Much of the activity involves state response to the 1986 changes in the Federal income tax law, to which most state laws are linked to some extent. More than two dozen states are expected to revise their income tax laws. Most will return to taxpayers any excess taxes that would result from their conformity with Federal law, but some will take advantage of the "windfall" increases.

But the bulk of the new revenues sought will come from other sources, chiefly general sales, motor fuels, and cigarette taxes. Twenty-five states are weighing tax increases that are unrelated to possible "windfalls." Only nine of those 25 states, plus four others, plan to retain excess receipts from Federal tax revision.

The changes under consideration, by type of tax, are summarized below, followed by a state-by-state summary of proposed revisions.

Personal Income Taxes

Personal income taxes will be the most revised type of tax in 1987. At least 22 states plan changes in their laws, and another state — Alaska — may levy a new income tax. Most of the states (19) will modify exemptions, deductions, and/or state rates and brackets so as to return all or a portion of the excess taxes that would otherwise result from state linkages to Federal law. These are: Arizona, California, Connecticut, Delaware (part), Georgia (part), Hawaii, Kansas (part), Maine, Maryland (part), Michigan, Minnesota, Montana, New York, Ohio (already enacted rate cuts in 1986), Oregon, South Carolina, Virginia (most), West Virginia, and Wisconsin.

On the other hand, at least 11 states plan to retain any "windfall" increases resulting from Federal tax revision. Three of them — Arkansas, Indiana, and Iowa — would revise their laws to do so, either by linking their taxes more closely to the Federal tax or by updating earlier linkages. Eight others are already linked to the "current" Federal Tax Code and need take no action to avert the "windfall." These are: Colorado, Idaho, Illinois, Louisiana, Missouri, New Mexico, Oklahoma, and Utah.

In addition to action or inaction in response to the Federal tax changes, several states plan base or rate changes in personal income taxes: Illinois (higher rates), New Mexico (limiting existing rebates), and Utah (repealing deductibility of the Federal tax). Reduction in rates (separate from action on the "windfall") may be approved in New York and in Rhode Island (where the tax rate is linked to Federal tax liability and has been adjusted to avoid a revenue loss).

North Dakota and Vermont have already raised their tax rates to avoid losses and Nebraska is planning other revisions to avoid losses.

Corporate Income Taxes

Fewer changes are under consideration concerning the disposition of "windfall" increases in corporate income taxes resulting from Federal tax reform. Two states — Louisiana and Ohio — took action in 1986 to avert any increases. In nine other states, governors have proposed that excess receipts be returned to taxpayers: Arizona, California, Maine, Montana, New York, North Carolina (where legislators are unlikely to go along), Oregon, South Carolina, and Wisconsin.

In another 12 states, governors and/or legislative leaders are recommending that the states retain any revenues resulting from Federal tax revision, often along with changes requiring closer conformity with the new Federal Tax Code. These are: Arkansas, Colorado, Florida, Georgia, Idaho, Iowa, Kansas, Minnesota, Missouri, New Mexico, Oklahoma, and Utah.

General Sales Taxes

General sales taxes are likely to be the source of the greatest revenue gains from legislation in 1987. Montana, one of only five states without a general sales tax, may enact one. Fourteen others expect to gain more money from the sales tax, either through base-broadening (sometimes coupled with rate cuts) or rate increases. These include: Arkansas, Florida, Idaho, Illinois, Indiana, Minnesota, Missouri, Oklahoma, South Dakota. Texas, Utah, Vermont, Washington, and West Virginia. Temporary increases in sales taxes may be extended or made permanent in Idaho and Texas.

Motor Fuels Taxes

The need for added highway funding is likely to lead to legislative increases in motor fuels taxes in at least 14 states. States considering such legislation include: Alaska, Florida, Idaho, Illinois, Iowa, Maryland, Michigan, Mississippi, Missouri, Montana, Nevada, New Mexico, Oklahoma, and Utah. Texas may extend a temporary increase.

Other Taxes

Seven states have reported plans to consider cigarette tax hikes: Idaho, Iowa, Montana, Nebraska,

North Dakota, Oklahoma, and Utah. In addition, ten states are considering other types of increases.

Alabama. The governor called for a serious study of the state's tax system so that a "meaningful and just" program of tax reform could be considered. The Alabama legislature does not convene until April 27.

Alaska. The governor proposed $425 million a year in higher taxes, including imposition of a personal income tax, higher taxes on motor fuels and the oil industry, and increases in various licenses and fees. He also urged repeal of the state's unitary tax on multinational corporations and of homeowner property tax exemptions. Because of declining oil revenues, deficits for 1986 and 1987, combined, are estimated at $875 million. Earnings of the Alaska Permanent Fund will be used to meet part of the deficit.

Arizona. The state's leaders favor adjusting state income taxes to avoid an estimated $140 million increase (personal and corporate) as a result of Federal tax reform. The governor has pledged to repeal the added 1 percent sales tax enacted in 1983.

Arkansas. The governor proposed new revenues totaling $185 million in 1988, largely for public schools. The funds would come from conforming state taxable income (individual and corporate) to the Federal Code, broadening the base of the sales tax, higher taxes on wine and beer, and other sources.

California. The governor proposed no tax increases and said that he supports greater conformity with the new Federal Tax Code, including fewer brackets and lower rates. There will be pressures to raise taxes (retail sales, excises) to obtain more money for education and highways, but the state is facing effects of a spending limitation approved by the voters in 1979; efforts are being made to ease the limit.

Colorado. The governor has asked the legislature to take no action to avert an estimated $200–$300 million personal and corporate Federal tax "windfall." The governor also expressed concern about the "dramatic shift in tax burden from state government to local governments" in Colorado.

Connecticut. The governor wants to continue taxing capital gains at the same effective rate as previously to avoid a $150 million "windfall" increase. Another large pending surplus is generating proposals for reducing the 7 percent sales tax and for offsetting the "windfall" rise in corporate income taxes, as well as for new and expanded spending programs.

Delaware. The governor has proposed tax adjustments as of January 1, 1988, to offset partially the Federal "windfall," by cutting the number of brackets from 14 to 9, by increasing the exemptions and standard deductions, and by reducing the top marginal rate from 8.8 percent to 7.8 percent.

Florida. The governor proposed reducing the sales tax rate from 5 percent to 4.5 percent along with extensive broadening of the sales tax base, and increases in insurance levies. He also asked that cities and counties be authorized to impose local option sales taxes of up to 1 percent. He urged that Florida's corporate income tax be revised to conform to the new Federal law. (Florida has no personal income tax.) The "windfall" from the corporate tax as a result of Federal tax reform is estimated at $58 million. Other likely tax increases include motor fuels levies.

Georgia. The governor announced his support for a measure that would bring the state's income tax system substantially in line with the new Federal law, and a law has been enacted to that effect. He suggested reducing personal income taxes by about $50 million (averting an estimated $250 million "windfall" from Federal revisions) by raising exemptions and standard deductions. The plan would raise corporate taxes by about $70 million.

Hawaii. The governor proposed a restructuring of the state's tax system, including changes in tax rates and brackets, to minimize the impact of Federal tax revision. He also asked for a $50-per-person food tax credit against income tax.

Idaho. The legislature has approved the governor's plan for making the "fifth cent" of the sales tax permanent. The governor also proposed that the state's personal and corporate taxes be conformed to the new Federal law (including repeal of the investment tax credit) and that the state retain the $22 million "windfall" that would result from conformity. Other proposals include increasing cigarette and motor fuel taxes. There is a question as to whether lawmakers will approve repeal of the investment tax credit.

Illinois. The governor's budget called for a $1.6 billion tax hike in fiscal 1988, to balance the state budget and allow higher spending for education, wastewater treatment facilities, and highways. His plan includes increases in personal income tax rates, broadening the sales tax base, and raising gasoline taxes and auto and truck license fees.

Indiana. The governor wants tax increases to support education. He proposed cutting the sales tax rate from 5 percent to 4.5 percent, while broadening it to cover services (for an additional $300-plus million over two years). The legislature is expected to approve the governor's recommendation for conforming personal and corporate taxes to the new Federal law and retaining the $50 million a year "windfall."

Iowa. The governor proposed significant changes in personal income taxes: eliminating deductibility for Federal taxes paid, reducing the number of brackets from 13 to 2. He also asked for a hike in motor fuels and cigarette taxes. Action is pending to conform the state tax to the new Federal Code and thereby raise state revenues by $145 to $190 million.

Kansas. The governor recommended minimal tax code changes in 1987, because of uncertainty over the actual impact of Federal tax reform on state revenues. He said that major reform could come later. Possible tax changes in 1987 include reductions in personal and corporate income tax rates and exempting manufacturing machinery and equipment from the sales tax. The state may return part — but not all — of the "windfall" increase from Federal tax reform.

Louisiana. The state constitution prohibits tax

increases in odd-numbered regular sessions of the legislature; a special session may be called to consider the governor's proposed hike in the state property tax. Louisiana expects to retain a 12.5 percent increase in personal income tax revenues owing to Federal tax revisions; adjustments to avoid effects on state corporate tax revenues were enacted in 1986.

Maryland. The governor proposed using most of the "windfall" from Federal tax reform for education and social programs and the rest for reducing taxes for lower-income persons. Legislative leaders, on the other hand, drew up plans to return nearly all of it to taxpayers. A compromise bill would return to the taxpayers about 68% of the estimated $178 million "windfall." The compromise contained provisions aimed at the poor, as well as retaining a 40 percent exclusion for capital gains. The governor also proposed an increase in the gasoline tax, to pay for highway improvements.

Massachusetts. The governor recommended updating the existing linkage in the state code to the new Federal Code. The revenue effect is expected to be negligible. The governor also proposed expanding the investment tax credit from 1 percent to 4 percent, with further restrictions on its use.

Michigan. The governor recommended a reduction in the state personal income tax rate from 4.6 percent to 4.4 percent to avert a $155 million "windfall." The motor fuels tax will probably be increased.

Minnesota. The governor proposed comprehensive tax reform, along with state tax increases totaling $629 million for the 1988-89 biennium. He would return an estimated $660 million "windfall" from Federal tax revision to the taxpayers. The governor's plan would raise corporate income taxes by $151 million for the biennium through closer conformity to the Federal tax, despite a rate reduction. Additional new revenues would come from broadening the sales tax base, from higher utility and insurance premiums, and other sources.

Mississippi. The governor called for no new or higher taxes. The legislature, however, overrode his veto of a bill to raise motor fuels taxes and license fees to pay for increased highway spending.

Missouri. The governor proposed higher personal and dependency exemptions for personal income taxes, but urged that no alteration in the state tax system be made in anticipation of a possible "windfall" from Federal tax reform, since amounts were highly uncertain. Other proposals would raise the rates of general sales and motor fuels taxes.

Montana. The legislature is likely to consider enactment of a general sales tax (Montana is one of only five states without one), along with hikes in taxes on cigarettes, tobacco, and motor fuels and new taxes on soft drinks, hotels, and motels. Legislation has been introduced to avert a "windfall" of $35 to $45 million from Federal tax revision, but the state faces such a deficit that the "windfall" is likely to be retained.

Nebraska. The governor recommended that the state's individual income tax (levied as a percent of Federal tax) be adjusted so as to yield the same amount as under current law. Lawmakers are leaning toward linking the state tax to Federal adjusted gross income and eliminating all itemized deductions except medical expenses. They have approved a cigarette tax hike.

Nevada. The governor proposed raising the tax on gross gaming revenues and retaining a 3 percent insurance premiums tax that is scheduled to expire. Other proposals would hike motor fuels taxes and increase motor vehicle registration fees. Local governments are said to be pushing for removal of current revenue-raising restrictions; and educators at all levels are reported to be seeking dramatic pay increases and higher taxes to support them.

New Hampshire. The governor proposed no tax increases. Hearings were held on a bill to cut the business profits tax from 8.25 percent to 7.5 percent on July 1, 1987, instead of to 8 percent as scheduled under current law; action has been deferred until 1988.

New Jersey. The governor proposed no tax increases. The state's personal income tax is not linked to the Federal revenue code.

New Mexico. The governor recommended increases in taxes and fees totaling $159 million, as well as state retention of an estimated $59 million "windfall" in personal and corporate income taxes that would result from automatic conformity to Federal law. The legislature has approved most of the governor's plan, which included increases in personal income taxes (limiting food and medical rebates), motor vehicle excises, gasoline taxes, and other user fees.

New York. The governor recommended legislation to return to taxpayers the $1.67 billion "windfall" from Federal tax reform. In addition, he proposed converting the state's sales tax on automobiles to an ad valorem tax which would be deductible in computing Federal tax; to administer the new tax, he would raise funds by increasing and broadening the state's mortgage recording tax in the Metropolitan Transit Region. In early March, the governor announced that he would support tax reductions totaling $1.7 billion over five years, beginning in 1987.

North Carolina. The governor said that he would like to return to the taxpayers any corporate tax "windfall" increase due to Federal tax revision, but legislative leaders appear unwilling to do so. The state's personal income tax does not conform closely to the Federal tax; current legislative proposals, however, would base the state tax on Federal taxable income.

North Dakota. In December 1986, the legislature raised the personal income tax from 10.5 percent to 14 percent of Federal tax liability, to more than offset an automatic loss from Federal tax reform and raise an extra $57 million over the next two years. (The hike came under fire and was referred to the voters, who approved it by a razor-thin margin.) The legislature has also approved a bill to raise the cigarette tax.

Ohio. The governor and legislative leaders have pledged that there will be no tax increases in 1987. Last December, the state enacted legislation to avert a $303 million "windfall" (in 1988) from Federal tax revision.

Both personal and corporate tax rates were cut. There is a trigger system in the law, however, designed to restore all or a portion of the personal income tax reduction in 1988 if the revenue impact of the Federal revision is 15 percent below the estimate for 1987.

Oklahoma. In March, the governor submitted revised tax proposals, recommending $248 million in higher taxes. He asked for increases in the sales tax rate and base and in the levies on motor fuels, cigarettes, and alcoholic beverages. Oklahoma is expected to retain the Federal "windfall."

Oregon. The governor asked for conformity to the new Federal Code, but "without nicking Oregonians for added taxes." "Windfall" receipts of $170 million a year are expected. The legislature is likely to reduce income tax rates, although there will be proposals to use some or all of the "windfall" to reinstate programs or establish a "rainy day" fund.

Pennsylvania. The governor wants to use nearly all of an estimated $261 million surplus for basic education. Opposition legislators are calling instead for cuts in personal and corporate income taxes. The state's personal tax is not linked to the Federal Code, but the state stands to pick up a "windfall" from the corporate tax unless changes are made.

Rhode Island. In 1986 the personal income tax rate was raised from 22.21 percent to 23.96 percent of Federal tax liability, to avoid a loss of $24 million in fiscal 1987. The governor has asked that the tax rate be cut, to save taxpayers $19 million in fiscal 1988.

South Carolina. Saying that the state's taxes had been raised 11 times in the past seven years, the governor proposed no tax increases and a new limit on general fund spending. In 1985, South Carolina conformed its state income taxes with Federal laws, and the governor wants to continue that linkage, with some adjustments.

South Dakota. The governor has signed legislation increasing the sales tax rate from 4 percent to 5 percent (for one year) and repealing the sales tax exemption for cigarettes.

Tennessee. The governor called for no new taxes and warned legislators that, if they want spending increased, they must come up with new taxes to pay for them. Absent action by the state, Federal tax reform will raise state corporate income taxes by an estimated $350 million over the next five years.

Texas. The state faces a $1 billion deficit at the end of the current biennium, and it is estimated that available revenues for the 1988-89 biennium will fall $5.8 billion short of the amount needed to retire the current deficit and adopt a "current services" budget. The governor has proposed continuing temporary general sales and motor fuels tax increases (for $2.9 billion in the forthcoming biennium), along with the sale of surplus state land and other nontax sources and fund transfers to augment general fund revenues. Attention is also being given to broadening the sales tax base to include services, as well as to raising the sales tax rate from 5.25 percent to 6 percent to raise $750 million for improving the state's prison system.

Utah. The legislature has approved most of the governor's proposed $200 million tax increase, including hikes in individual income taxes (by denying Federal tax deduction), motor fuels, general sales, and cigarette tax rates. The state expects to retain most of a $58 to $60 million Federal "windfall."

Vermont. An increase in the personal income tax rate — from 25 percent to 25.8 percent of Federal tax liability — has been approved. Legislative leaders have been moving toward an increase in the state sales tax to boost aid for poorer school districts.

Virginia. Legislation approved in February will return to personal income taxpayers about $145 million of an estimated $173 million "windfall" from Federal tax reform. The new state law increases the standard deduction and personal exemptions and raises the threshold at which the lowest and highest rates apply. For corporations, the law recoupled state provisions with Federal asset depreciation schedules. The governor said he would earmark the remaining $28 million of the "windfall" as a special "tax reform reserve," to be returned later if revenue estimates prove accurate.

Washington. The governor proposed tax increases totaling $510 million over the next two years in state taxes and $272 million in local taxes. The new funds would be used to finance education improvements. The governor's plan includes broadening the base of the sales tax to include most services, while reducing the rate from 6.5 percent to 6 percent. Other changes involve revisions in the business and occupation tax.

West Virginia. The governor proposed returning to taxpayers $24 million of an estimated $47 million "windfall" from Federal tax reform and using the rest to help balance the budget. The legislature, however, approved a bill — awaiting the governor's signature — that would return all of the "windfall" and raise taxes by $43 million, mainly through taxing more business purchases under the sales tax. Lawmakers also approved a new payroll tax on employers and workers to help pay off the state's large debt to the Federal unemployment compensation fund.

Wisconsin. The governor proposed that the state income tax be conformed in most respects to changes in the new Federal law. He would use the estimated $164 million "windfall" from the personal income tax to cut rates across the board by 3.5 percentage points, to retain the 60 percent capital gains exclusion, and to phase out the inheritance and gift taxes over four years. He asked that the state's corporate income tax also be conformed to the Federal changes, but in a revenue-neutral way. Opponents of the governor's plan want to double the governor's proposed personal income tax cut, but pay for it by taxing 100 percent of capital gains.

Wyoming. The governor asked for a constitutional amendment to establish a controlled, limited tier (classified) system of property taxation, with a limit on the allowable difference between tiers. He also called for changes in taxation of natural resources.

(MEDICARE, *from page 2)*
situation, however. Rather than shrinking, Medicare spending is $30 billion higher than it was just five years ago. While some cutbacks have been made, the spending escalation has not been halted. Here are some reasons why Medicare grows when it is cut:

• The size of the cuts has been greatly exaggerated by Congress. Increases in Medicare premiums are lumped together with program changes in computing the size of the cuts. The justification for this is that both increased charges and program cutbacks contribute to deficit reduction. But this practice creates a misleading impression of much deeper cuts than have actually been made.

• The cutbacks are computed in terms of a hypothetical baseline of the amount of spending that would occur if no program changes were made. The baseline projections enable Congress to define rising expenditures as program cutbacks. The baseline assumes the inflation and utilization rates expected in health care over the next several years. Savings are realized only to the extent that these assumptions turn out to be valid. It is highly probable that savings have been substantially overstated in recent years.

• Congress is very adept in counting temporary changes as permanent savings. When it froze hospital payments for one year and physicians' fees for 15 months, Congress took credit for billions of dollars in deficit reduction, even though it did not cut a single dollar from the Medicare budget. Temporary cuts — unlike permanent ones — can be double-counted: first when the temporary provision is enacted; and again when it is renewed.

• Congress has resorted to gimmicks that produce paper savings without really cutting expenditures. It can defer payments from one year to future years and count the lower spending as a cutback. A few years ago, for example, Congress tampered with the Julian calendar by providing that Medicare would have 11 months in fiscal 1981 and 13 months in fiscal 1982.

• There is growing evidence that the recent changes in Medicare have resulted more in behavioral changes by providers of health care than in dollar savings. Despite freezes in hospital payments and a shift from cost reimbursement to a prospective payment system, the profit margins of hospitals for Medicare services have been much higher in the past few years than before these assumed cutbacks were made. Despite freezes and caps on physician fees, the cost of this part of Medicare is also rising much more rapidly.

The Medicare Time Bomb

Medicare is a "time bomb" that threatens to bankrupt the system of health care for the elderly. At the present rate, the Medicare trust fund will run out of money around the turn of the century and huge tax increases or transfers from the Social Security trust fund will be required to keep it afloat.

The inflationary conditions that have beset Medicare are likely to persist and possibly worsen in the future. The elderly -- especially those over 75 — will constitute a growing portion of the population, and the utilization of medical services — especially long-term care in nursing homes and other expensive facilities — will increase. Congress is likely to enact a catastrophic health insurance plan this year, and many see this as opening the door to further expansions in the years ahead.

Demographic changes will impel large spending increases in Medicare, but the size of these increases can be moderated by more realistic congressional budget actions:

1. Congress should not exaggerate the size of cutbacks and should stop counting bookkeeping tricks as deficit reductions;

2. Congress should base program improvements on realistic cost estimates. The history of Medicare has consistently shown costs exceeding estimates made out of political expediency;

3. Congress should trade off program improvements for changes in the current structure of Medicare. One option would be to have patients pay a higher share of the cost for routine care while increasing the government's assistance for acute illness.

Past performance offers little grounds for optimism that Congress will take these steps. But Medicare is a program that may be running out of miracles. If it does, and if the Congress fails to act in time, the verdict will be, "The program was successful but the patient couldn't afford to pay the bill."

THE FRONT BURNER

By Robert C. Brown, President
Tax Foundation

"The Circle Closes"

Each year Tax Foundation economists calculate how long the typical worker must spend on the job in order to meet Federal, state and local tax obligations. They do this, not out of a perverse desire to engage in tax-collector bashing, but because the Foundation's fundamental reason for being is to educate the American taxpaying public on the size and weight of government on the overall economy.

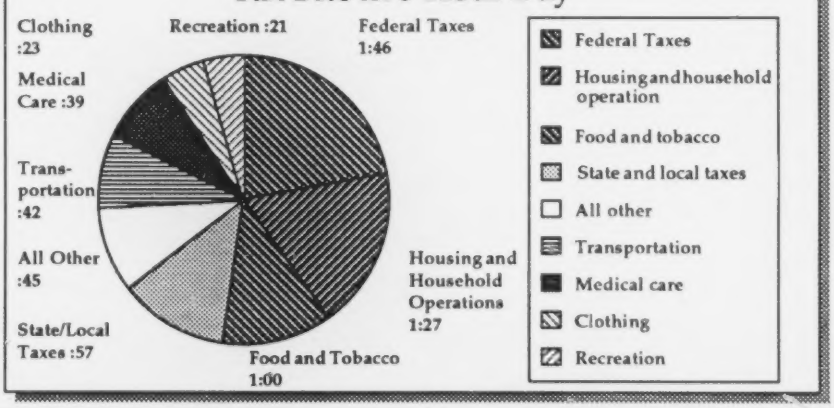
This year, the news is not pleasant. In 1987, the average American will spend 2 hours, 43 minutes on the job to keep the tax collectors happy. This puts us exactly where we were in 1981. It has taken just six years to undo the revenue giveback of ERTA, the so-called Reagan tax cut. The good new is that without those cuts, we'd be working even longer for the tax man.

The circle has closed — but with a difference. In 1981, the average worker spent 1 hours, 52 minutes to pay Federal taxes and 51 minutes to pay state-local levies. This year, the ratio shifts to 1 hour, 46 minutes for Uncle Sam and 57 minutes for the states and localities.

The shifting in funding of a number of Federal programs has helped move the tax burden from Washington closer to home. State and local officials and taxpayers must now choose which of those programs they want and must find ways to pay for them. Quantitatively, they have chosen to pick up virtually all the costs Uncle Sam has laid down. There have been changes in priorites although space does not permit us to detail their extent.

Two fundamental principles of public finance, however, remain intact: There's no free lunch. You get what you pay for and, conversely, sooner or later, you pay for what you get.

Tax Bite in 8-Hour Day



ESTIMATED TOTAL AND PER CAPITA FEDERAL TAX BURDENS BY STATE, FY86 — FY88

State	Total Burden (Millions)			Per Capita Burden			Rank 1987	
	1986	1987	1988	1986	1987	1988	Total	PerCap
TOTAL	$744,578	$818,856	$894,258	$3,090	$3,365	$3,639	—	—
AL	9,340	10,227	11,167	2,311	2,515	2,731	24	43
AK	2,394	2,595	2,830	4,377	4,520	4,693	44	4
AZ	8,944	9,876	10,804	2,725	2,920	3,100	26	33
AR	5,038	5,558	6,077	2,136	2,355	2,574	32	49
CA	92,012	101,362	110,712	3,422	3,694	3,954	1	11
CO	10,588	11,657	12,734	3,210	3,462	3,704	23	13
CT	14,281	15,674	17,117	4,485	4,904	5,337	17	1
DE	2,251	2,462	2,692	3,590	3,896	4,220	46	8
FL	35,440	39,348	42,997	3,031	3,269	3,470	6	23
GA	16,266	17,869	19,545	2,678	2,893	3,112	13	34
HI	3,082	3,395	3,715	2,878	3,118	3,356	40	26
ID	2,332	2,575	2,814	2,295	2,505	2,706	45	44
IL	39,545	43,441	47,393	3,425	3,757	4,093	4	9
IN	15,229	16,757	18,317	2,771	3,049	3,333	15	29
IO	7,605	8,432	9,210	2,644	2,939	3,217	28	31
KS	7,491	8,260	9,027	3,039	3,329	3,615	29	20
KY	8,396	9,241	10,090	2,248	2,466	2,685	27	46
LA	11,336	12,418	13,546	2,530	2,770	3,020	22	37
ME	2,845	3,140	3,431	2,429	2,666	2,895	42	40
MD	16,764	18,361	20,056	3,791	4,122	4,469	12	5
MA	21,764	23,938	26,147	3,731	4,093	4,460	10	6
MI	28,534	31,248	34,061	3,154	3,467	3,795	9	12
MN	12,880	14,204	15,535	3,058	3,355	3,651	20	18
MS	4,896	5,375	5,870	1,862	2,031	2,204	33	51
MO	14,838	16,383	17,910	2,941	3,234	3,521	16	24
MT	2,000	2,213	2,417	2,401	2,634	2,851	47	41
NE	4,491	4,980	5,455	2,786	3,078	3,359	34	28
NV	3,124	3,419	3,722	3,241	3,443	3,641	39	15
NH	3,458	3,804	4,160	3,414	3,701	3,988	38	10
NJ	31,909	35,008	38,197	4,202	4,588	4,983	8	3
NM	3,481	3,825	4,183	2,354	2,535	2,718	37	42
NY	64,161	70,716	77,271	3,602	3,962	4,320	2	7
NC	15,939	17,476	19,093	2,521	2,732	2,951	14	38
ND	1,790	1,976	2,156	2,591	2,835	3,067	48	35
OH	32,030	35,179	38,411	2,986	3,284	3,591	7	22
OK	9,106	9,975	10,881	2,716	2,926	3,141	25	32
OR	7,298	8,059	8,802	2,708	2,979	3,243	31	30
PA	36,306	39,848	43,454	3,066	3,367	3,674	5	17
RI	3,059	3,363	3,671	3,150	3,449	3,749	41	14
SC	7,523	8,259	9,031	2,220	2,406	2,597	30	47
SD	1,586	1,766	1,935	2,230	2,473	2,699	49	45
TN	11,984	13,141	14,365	2,501	2,725	2,959	21	39
TX	52,461	57,402	62,665	3,123	3,328	3,539	3	21
UT	3,666	4,024	4,398	2,181	2,341	2,502	36	50
VT	1,384	1,526	1,664	2,567	2,805	3,036	51	36
VA	18,228	20,065	21,946	3,158	3,435	3,711	11	16
WA	13,718	15,079	16,448	3,076	3,341	3,601	18	19
WV	4,135	4,542	4,955	2,140	2,356	2,574	35	48
WI	13,448	14,816	16,168	2,811	3,089	3,363	19	27
WY	1,537	1,684	1,837	2,978	3,215	3,453	50	25
DC	2,660	2,906	3,168	4,270	4,680	5,125	43	2

Source: Total taxes as shown in the Federal budget submitted January 1987; computations of total and per capita tax tax burdens by state were made by Tax Foundation.